

Oct. 26, 1994

LETTER 1159

"A bear market tests your stomach, your pocket book, your sanity -- and always your patience." -- Richard Russell.

THE DOLLAR: *"Down it goes and where it stops nobody knows."* Oct. 14 -- the US Dollar Index breaks below 87, sinking to its lowest level since September 1992.

STILL BULLISH AFTER ALL THOSE LOSSES: There really does seem to be an ingrained bullish psychology among the nation's investors. I could make a montage a mile long out of currently bullish brokerage reports, advisory letters, news clippings and predictions by "perma-bull" advisors. I include a tiny sampling below.

Lynch predicts long run for bull market

More than four years have passed since Peter Lynch retired as head of Fidelity's mammoth Magellan stock mutual fund. Lynch, 50, pronounced the market is earnings will be good for several years. He expects Standard & Poor's 500 to rise 56 points to 3877. Lynch told USA TODAY why the bull market will run through 1997: "The economy will not stall and drive down."

Buy Signal For Global and U.S. Stock Markets!

Dow 4600 Ahead! *"The Next 10 Years Will Be the Best in History!"* Lynch says the market is earnings will be good for several years. He expects Standard & Poor's 500 to rise 56 points to 3877. Lynch told USA TODAY why the bull market will run through 1997: "The economy will not stall and drive down."

• Dow to Hit 7000 by Year 2000

You have to ask yourself why, with most stocks well off their peaks, the public and the pros continue to be hopeful if not outright bullish on the market. The answer lies in the **action of the Dow**. Despite hundreds of billions of dollars in stock and bond losses, the Dow has managed to hold within 2-3% of its 1994 high. And we all know that when TV or radio commentators talk about the "market," in reality they're reporting on the latest price of the Dow.

In the last Letter I discussed the "reverse wealth effect," or the effect that a generally declining market exerts on both investors and consumers. Probably the **indicator that most closely dovetails with the wealth effect is the NYSE advance-decline ratio**. When that ratio heads down on a trend basis, it tells us that more stocks are declining than advancing over an extended period of time. In turn, that action tells us that people are losing money, bundles of it.

The A-D ratio (NYSE) peaked on February 2, 1994, and it's traced out a series of lower peaks and lower lows ever since (see page 2 chart). This is the real trail of the bear. However, what's remarkable is that with the A-D ratio declining over the last eight months, people are still basically optimistic regarding stocks. But, of course, that's exactly the way the bear wants it -- "keep 'em happy and losing money." Is this a "fun bear market" or what?!

THE FUNDS: The outstanding phenomenon of this bear market is the insistent, massive, never-ending buying of mutual funds by the public. Through August of this year, a whopping \$98 billion of public money has flowed into equity mutual funds (a new record for any first eight months of any year). In August alone \$14.4 billion poured into equity mutual funds, up from \$9.7 billion in July and up from \$12.5 billion in August of 1993.

What this means is that the American public remains stubbornly optimistic. Moreover it means that the public has assumed the most massive position in the stock market ever. All very exciting. But

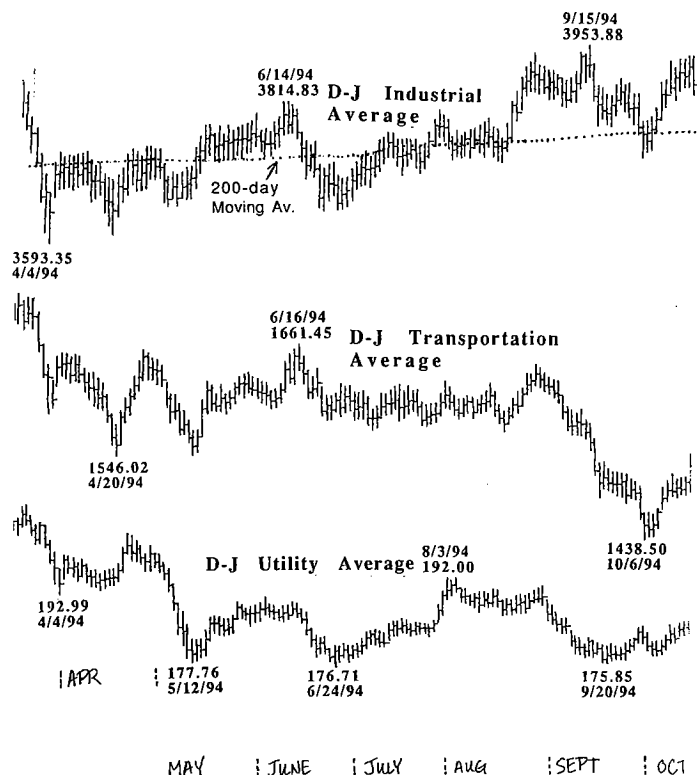
Oct. 14 DJIA 3910.47; PTI 4011; A-D Ratio -7.08
Oct. 21 DJIA 3891.30; PTI 3990; A-D Ratio -7.66
Dow Yield: 2.72%; Dow Price/Earnings: 20.0
Dow 200-day MA: 3795; Dow 30-day MA: 3870
Dow Times Book Value: 3.48; PTI 89-day MA: 4016
Percentage of Undervalued Blue-chips: 11%
Dow Low Risk Buy Index: +42; Gold-PTI: 984
Gold 200-day MA: 385

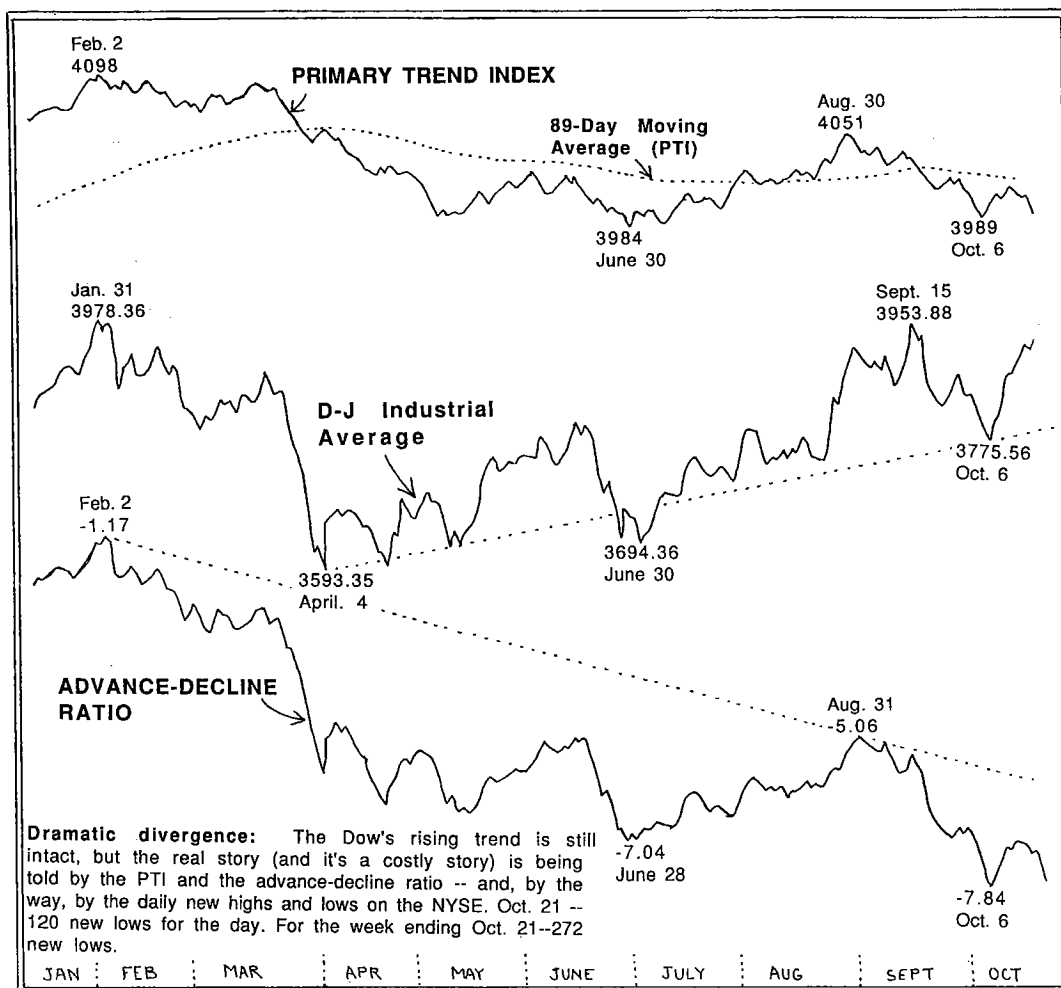
what I don't like is this -- as the bear market wears on, the losses and the "reverse wealth effect" are going to be devastating.

In a fascinating study, Alan Newman (analyst at HD Brous & Co., Great Neck, NY) took the net money inflow into mutual funds on a cumulative basis and divided it into the S&P (the S&P is a proxy for two-thirds of the market's capitalization). Newman states, *"You will find that it takes more and more money to drive stocks up one point at a time. The last \$130 billion has brought almost zero price appreciation. The way I see it, all the continuing money inflow can do is help support prices. It cannot buy price appreciation."*

That's an ominous observation. It means that billions and billions of dollars of public money flowing into the funds have only produced "churning." But remember this -- **the primary trend of the market is more powerful than all the money the public is pouring into the funds**. And if I'm correct, if this is indeed a primary bear market, then the funds are fated to decline and the public is fated to sustain major losses.

So far, the equity funds have merely backed off while the bond funds have been hit hard. But what happens if the equity funds begin to decline in earnest? What happens if the public decides that





it's had enough? What happens if the public panics and rushes to bail out of its massive mutual fund positions? When that happens, the bear market will move out of its current first phase and into its second phase.

That second phase should be historic. It should be terribly costly. It should be frightening. It will undoubtedly raise doubts about the entire mutual fund industry. And it will also bring about (I believe) a thorough review and questioning of the whole socialistic, big-government, welfare-state trend which has increasingly dominated this nation since World War II (actually, this is being questioned now).

This is from Martin Zweig's *Forecast* (PO Box 360, Bellmore, NY 11710): "Let's try a quiz. Starting in 1983, the S&P Index has produced a total return of 407% or some 15% a year. Name two things that have gone up more. The first answer is the number of mutual funds, which have expanded by 627%, to a total of 4,000 (which is greater than the number of stocks on the NYSE). That's a growth rate of 18.6% a year. The second answer is the percentage of mutual funds per household assets. This ratio has expanded from about 2% to 17%, a gain of 750% or 20.2% a year."

On page 2 I've included a chart of the Dow, my Primary Trend Index and the NYSE advance-decline ratio. The chart is really self-explanatory. What we see here is a rather dramatic picture of a "strong" Dow, a weak, down-trending PTI and a bear market in the A-D ratio. History tells us that the Dow (in its own good time) tends to get in harmony with any persistent trend in the PTI and the A-D ratio. The fact is that the Dow has been "out-of-gear" with the PTI and the A-D ratio ever since early April (again, study the page 2 chart).

It's actually as if two markets exist. On the one hand we have the Dow market, the blue-chip market made up of giant, highly

capitalized stocks. On the other hand, we have the rest of the market, comprised of typical stocks that for any number of reasons are (in the majority) heading down. It's clear that the great unconscious of the market is dealing with "something it doesn't like." That something has not yet impacted on the Dow. In due time it will.

What could that "something" be? Here are my guesses: (1) deflation; (2) rising interest rates; (3) a collapse of the dollar; (4) a forthcoming recession. Take your choice. My choices -- any one or even all four.

Note: The ratio of coincident to lagging indicators has been declining since March. Declines in this ratio have foreshadowed economic recession on an average of about 13 months (which is far earlier than the index of leading indicators). This suggests that a recession could begin around the first quarter of 1995 -- and remember, the stock market moves before the event.

INVESTMENT POSITION:

Surprise, it's still a bear market; therefore, the bear remains in the box. You like fun and excitement? Then play the game of "beat the bear." That entails reading the advice of the experts, buying the stocks that they say are fated to go up. Or if you'd rather, try in-and-out trading in an effort to catch the rallies.



Of course, you can also elect to follow **correct bear market procedure**. That entails getting liquid, staying on the sidelines, reading your *Wall Street Journal* -- and giving yourself and the market a rest.

If you've been brilliant, you've had your money in Swiss francs or D-marks or yen, all of which moved up better than 12% against the dollar in '94. If you've been merely smart you've stayed largely in cash while holding some gold or gold stocks. If you've been adventurous and lucky you might have picked a few winning stocks while avoiding the many losers. If you've been a died-in-the-wool optimist, you're holding a losing hand while praying that it's still a bull market.

But as I've said many times, I advocate correct procedure. Correct procedure tells us to get liquid and avoid the nonsense of trying to beat the bear. Why buck the odds? If you play long enough in Las Vegas or Atlantic City, the house is guaranteed to take your money. That's what they're in business for -- to take your money. The bear is in the same business. Ah, but you may have to find that out the hard way.

Investment Quality Trends here in La Jolla is an expert on stock valuations. Of the 30 Dow stocks, they list 19 as both overvalued and in declining trends. They list only two Dow stocks in the undervalued and already beaten-up category, Merck and Philip Morris. Dow stocks that are both overvalued and in declining trends include Alcoa, Allied Signal, AT&T, Caterpillar, GM, Goodyear, IBM, IP, McDonalds, Union Carbide, United Tech., Westinghouse.

FED UP: In an ABC News survey last week 53% of those polled said they were dissatisfied with the way the federal government works and 19% said they were just plain angry at the government. That adds up to 72% who said they are fed up with government.

THE SAN DIEGO UNION-TRIBUNE

Friday, October 14, 1994

72% fed up with U.S. government, poll says

ASSOCIATED PRESS

WASHINGTON — Nearly three-fourths of Americans are dissatisfied with the way the federal

in the survey's margin of error, meaning it was a statistical dead heat, Republicans have not fared that well on such a generic question.

However, the ABC and other recent polls with larger samples have found a smaller Republican advantage or statistical dead heat in the

the way Clinton was handling the Haiti situation. Forty-three percent approved.

U.S. Voters Cynical and Dispirited

By Richard L. Berke
New York Times Service

SAVANNAH, Georgia — This colonial city is sedate, but get them talking about politics, and residents here are no less irritable, dispirited or cynical than the rest

"The hope and the expectations of 1992 have given way to the fear and cynicism of 1994," said Peter Hart, a Democratic pollster. "It is really surly and mean."

What is also striking, as well as perplexing, is that unlike the situation in the past

Graves, 53, a retired fire fighter and an independent, said he was thinking of moving to California because of what he described as a crime rate and more favorable tax

In other words, three out of four Americans have "had it with Washington," and this in the face of a fairly decent economy, no shooting war, high factory utilization and good statistics on employment. So I ask myself, "Why are three out of four Americans angry and disgusted with government?"

First, let me voice my own anger. I'm paying (state, city, federal) taxes of almost 50% of my earnings. And what do I get for it? *Big government* is the only thing I can come up with. Second, I feel the government is sticking its nose into and getting in the way of just about everything I do. I get forms, rules, red tape, annoyances, aggravations at every turn. Finally, the more I see of our so-called representatives in Washington, the angrier I get. They've been there too long, they're out of touch with my problems, they live by different rules and laws than I do and I don't understand their obsession with getting re-elected. It's like a disease. Why are they all so damned anxious to stay in Washington? Why will they spend hundreds of thousands of dollars, in some cases millions of dollars, to hang on to their jobs? The only thing I can think of is power, power, power, perks -- and more power. Yuck.

A few interesting statistics. In 1930 the personal staff of the House members was 840. In 1947 it had increased to 1,440. By 1991 it had rocketed to 7,278. On the Senate side the staff was 280 in 1930, 590 in 1947. In 1991 it had exploded to 4,294. For what? The Supreme Court gets Congressional appropriations to run their office to the tune of \$24.6 million. The Executive office (President) gets \$298 million. And the Congress gets \$1.6 billion. What, \$1.6 billion to the Congress? Sounds high to me. Sounds outrageously high, in fact.

Did you know that government (states, fed, cities) now employ more people than all the manufacturing workers in the US? Did you know that government now spends more than 40% of the US Gross National Product? The public may not be aware of the actual statistics, but they sense that the government has become a veritable monster. And it's a monster that gets in our hair. The voting public (you and I) know that we are supporting a massive army of government workers numbering over 18 million. And we resent it. I know I do.

Further resentment stems from the entire welfare system. The general perception is that one-half of the US population supports the other half (that may be an exaggeration, but believe me it's a widely held perception). And people resent it. Here in California, Proposition 187 is going to pass -- pass BIG. This is the Proposition that mandates that the state stop paying for medical, schooling, etc. for undocumented aliens (and California is

swimming in them). The state pays over \$2 billion a year for aliens who cross our border and live here illegally. Residents of the "Golden State" want it to end.

Finally, it's obvious that an awful lot of people resent Bill Clinton, what he is, and what he stands for. What he is -- is duplicitous and a womanizer. (I should call him a "closet womanizer," since he never admits to anything.) What he stands for is BIG government, government solutions for problems, government, government and more government. Clinton campaigned as a middle-of-the-road Democrat but he deceived the voters. It turned out he was a far-left Democrat. Clinton wasn't what he pretended to be and his thousand-page "health bill" finally revealed to Americans what Bill and Hillary were all about.

The health bill was jettisoned, which is what I expect will happen to a lot of Democrats in November and to the Clintons in 1996. If I'm wrong, well, we'll just deserve what we get, which will be four more years of the couple from Arkansas.

NOTES & QUOTES: I wish subscribers could see my mail. There's just no way in the world I can answer all the letters and questions that come in each day. In addition to the questions, it's incredible the number of comments and interesting stories that arrive here. Whatever I discuss (particularly in Notes & Quotes) draws letters, and the story in the recent Letter about the Smithsonian exhibit (atomic bomb) was no exception -- I received letters from angry ex-airmen from all across the nation. It seems that no matter what I write about there are subscribers out there who have "been there," "done that" or are truly experts on the subject. One time I wrote something about leprosy, and darned if I didn't get a letter from a priest-subscriber who was working in a leper colony in West Africa. Hard to beat that one. Although I can't answer all the letters, I appreciate receiving them, particularly the ones offering information and news clips. Many, many thanks.

Which reminds me, I just received a letter and a large amount of fascinating information from subscriber Chalmers H. Goodlin, Chairman of the Burnelli Corp. of Miami, Fla. The story of the avoidance of the great, safe Burnelli design for aircraft is a disgrace; it's beyond belief. My old buddy, Harry Schultz, has been writing about the Burnelli design for years. Burnelli submitted designs for vastly safer aircraft based on an air-foil fuselage and much safer positions for gasoline storage. The designs have been denigrated and avoided by the government and major aircraft manufacturers for decades. Congressmen and aircraft makers who read this should contact Burnelli for information [FAX -- (305)592-3273]. After reading Mr. Goodlin's letter and material, I'm tempted to never again fly in one of today's planes.

Why in the world did Saddam Hussein move 60,000 troops to the border of Kuwait? Was he going to invade Kuwait again? Not a chance. Then what was he thinking about? Gen. Norman Schwarzkopf has the answer. "The most plausible reason," stated the general, "is the Jimmy Carter factor." Saddam was hoping that Clinton would send in wimpy Jimmy Carter to work up one of his "give-away" compromises and perhaps lift the sanctions. It didn't work, but you've got to admit it was a ploy worth trying as far as Saddam was concerned. Remember, our "surrogate Secretary of State," Jimmy Carter, never met a dictator he didn't like. Which has some of us wondering if there isn't some way of getting Jimmy back to Georgia, hopefully out of trouble and planting peanuts again.

The N. Korea "nuclear settlement" -- \$4 billion in US goods. The Haiti "settlement" -- a US gift of \$60,000 in rental payoffs to killer Cedras and a first-class plane trip to another paradise.

Does the public make money in the stock market? As a rule, no. *Morningstar* recently ran an analysis of the total returns on 219 growth funds which were tracked for the five-year period ending 5/31/94. The analysis compared the average fund's annual return (in other words, the return the fund itself generated) with the return the investors actually come up with.

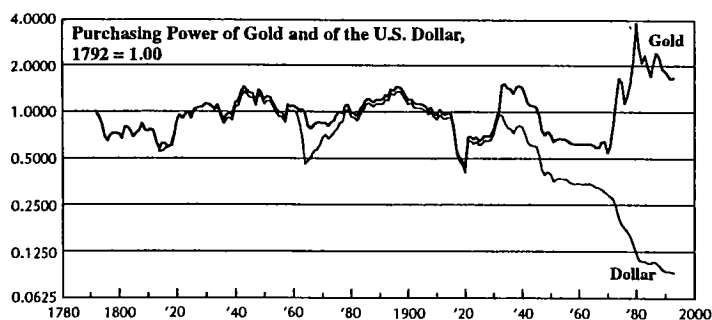
What they discovered was amazing. The funds themselves over the five-year period returned 12.5%. But the returns to the individual

investors was a **negative 2.2%**. How could this be? (1) Investors panicked out of their so-called "long-term investments" during severe market declines. (2) Investors rushed back into the funds too late -- or long after the best gains in the funds had been realized. In other words, fund-buyers get frightened out of their "long-term holdings" during a market decline, and then they come back after the funds have made substantial recoveries. Result -- net losses to investors.

Today we see fund holders hanging on and then buying more, even though most stocks and the funds themselves have declined. Ironically, maybe investors have learned their lesson too late. This time they'll hang on to their funds for dear life -- in the face of a major bear market.

Ruble: October 12 saw the ruble drop a disastrous 21% against the dollar, down to almost 4000 rubles to the dollar. The collapsing ruble is resulting in galloping inflation in Russia. The situation is demoralizing for both the consumer and business. As subscribers know, I stated as soon as the Communists were overthrown that the Russians should move to a **gold-backed ruble**. But under advice from a number of Harvard professors, the ruble was issued as a fiat (nothing behind it) piece of paper. The only thing holding up any fiat paper is confidence. Wrote the *WSJ* (Oct. 12), "The ruble's stunning decline mirrors larger woes in Russia's economy. The main problem is excessive granting of credits by state banks to state farms and enterprises. After achieving some success in taming inflation, the government loosened its monetary policy this past summer, adding to inflationary pressure undermining the ruble." **Russell comment:** Without the discipline of gold, ALL paper currencies lose purchasing power. It isn't a question of whether, it's a question of HOW FAST. In Russia, it's been very fast.

This chart traces the purchasing power of the dollar vs. gold. The dollar isn't the ruble, but the direction of the dollar's purchasing power is the same -- down. The trip's just taking a lot longer. Since 1940 the dollar has lost 90% of its purchasing power. And I can testify to that. In 1940 I could buy a full course meal in a better NYC restaurant for \$1.50. Today that same meal would cost me upwards of \$60. (Chart courtesy of *American Investment Service*, Great Barrington, MA 10230.)



Contrary Opinion: Marty Zweig notes that the number of bullish *Barron's* ads (three-week total) has soared to an all-time record of 96, this based on 24 years of back-data. He notes that at the June 1982 market low the total was minus 2. "The peak of pessimism was a minus 54 reading in September, 1974, just days before the bottom of the worst bear market since the 1930s."

Wrong Guess: Even legendary investor Warren Buffett of Berkshire Hathaway can lose money. Buffett bought \$359 million worth of the US Air Group. *Fortune* estimates his loss at \$200 million. But who cares -- Buffett is the nation's second richest man, his fortune estimated by *Forbes* at around \$9 billion.

Katzenberg, Geffen and Spielberg, three multi-millionaire, multi-talented college dropouts. The three are getting together to start a new film studio. I think it's going to work. I think it will be a major success. I also think the stupidest thing Michael Eisner ever did was push Katzenberg out of Disney. I don't think Disney knows which way or where to go now. I also think they've created

a tough competitor. Personally, I wouldn't touch Disney's stock at this point.

I received a number of letters regarding my negative comments on the unchecked growth of the world's population. I stick by my guns -- there are just too many people on earth and the problem (and it is a problem) is getting worse. Consider this -- the recent world population conference in Cairo took place over **nine days**. During those nine days the world population **grew by 1,893,400**. Here's a very partial breakdown of where the growth was: Egypt 28,000, US 57,000, Bangladesh 57,000, Brazil 57,000, China 275,000, India 374,000.

What are the chances of Aristide remaining as president in Haiti or of Haiti opting for democracy? Not that great. Here's the record of Haiti's rulers just since 1930. Stenio Vincenta (1930-41), **resigned**; Elile Lescot (1941-46), **fled to Florida**; Eumarsais Estime (1946-50), **overthrown**; Paul Magloire (1950-56), **overthrown**; Nemours Pierre-Lois (1956-57), **resigned**; Franc Sylvain (1957), **overthrown**; Daniel Fignole (1957), **overthrown**; Francois Duvalier (1957-71), **died of illness**; Jean Claude Duvalier (1971-86), **fled to France**; Henn Namphy (1986-88), **stepped down**; Leslie Manigat (1988), **overthrown**; Henri Namphy (1988), **overthrown**; Prosper Avril (1988), **fled**; Pascal-Trouillot (1990), **taken hostage**; Jean-Bertrand Aristide (1991), **fled to America**; Cedras Junta (1991-94), **bought off by the Carter Clinton combo**, and flown away with his family to a better life in a better land.

Lazy Americans? Americans have one of the highest living standards in the world. How do they do it. One way is via debt -- Americans borrow what they need for the good life. Secondly, they work long hours. A recent study found that Americans work an average of 38 hours a week, two hours longer than the 36 hours that the average German works. And, of course, in many families both the husband and the wife work. Americans put in 130 hours a year more than the average number of hours worked by the average European.

Did you see Larry King's nutty interview with Marlon Brando? Marlon, Marlon, what have you done? You must weigh 350 pounds and be 65 inches around the middle. According to a source on the set of *Don Juan de Marco*, in his upcoming movie with Johnny Depp, Brando "gained an entire suit size; a new suit had to be made for him." Remember the old reverse-adage, "A waist is a terrible thing to mind."

Sign of the '90s -- the caption of a cartoon in the current *New Yorker*: two girls are talking, one tells the other, "I'm in love with a married man who -- just my luck -- is in love with a married man."

California's Congressman, Chris Cox, recently introduced a bill which would eliminate the Post Office's monopoly on first class mail. The PO is requesting a 10.3% across-the-board increase to meet the cost of stiffer competition. What a disgrace. In private industry when a company faces tough competition, it cuts its prices. Not so, the PO monopoly. They just keep running deficits and raising the price of stamps. And more nonsense -- when faced with the call for private competition, the PO argues that it delivers mail everywhere, including all rural areas, and private industry will not do that. Baloney, United Parcel Service delivers everywhere. **Russell prediction** -- E-mail, FAX and electronic communication are going to push the PO to the wall, and in due time the pressure to privatize the PO will be overwhelming. But why wait and pay and pay -- let's get it done as soon as possible.

Showtime (owned by Viacom) has announced that it will commission 40 original movies to run in 1995. They will back the program with \$150 million. This will make Showtime the biggest producer of independent movies in the world. I think it's a great idea and it will give a lot of talented writers, directors and actors a chance to show their stuff. I've seen many of the low-priced Showtime originals, and quite a few of them are very good (as are so many of the HBO originals).

Well, I signed up for one. I'm talking about the new DSS (digital satellite system). The 18-inch satellite dishes are here, and even Sears is selling them. Installation cost is around \$700 to \$900. They'll bring in 75 digital stations and they have a capacity for 150 stations. Cost seems to be around \$30-plus a month for Showtime, HBO, Cinemax, 17 movie stations. They're working on a full sports extra for what I understand will cost extra. This has to be vicious competition for cable. And for areas without the cable, it will be an absolute winner.

Dollars: Despite its years of sagging, the world still collects 'em. The world's central banks hold 60% of their reserves in dollars, or about 60% of their total reserves. Twice as many dollars are floating around outside the US as are in the US. Seven out of every ten \$100 bills reside outside the US. Many nations literally use dollars as their real currency. Item: the Russians have more words for the dollar than the lowly ruble -- *baksi* (bucks); *zelyonyike* (green); *kapusta* (cabbage); *krop* (dill); *zelon* (green herbs). BUT -- although the greenback is used in 83% of all foreign exchange dealings, this is down from 90% in 1990. In 1988 36 nations pegged their currency to the dollar, today the number has dropped to 20. And the percentage of dollars held by central banks as reserves continues to decline. Conclusion: the dollar is still loved, but loved less and less as the years go by (whereas the yen and D-mark are loved more).

The Russian mob must be making money. Louise Esterhazy, writing from Zurich for the October issue of *W*, observes, "What on earth were they (the Russian gangsters) doing in the Baur au Lac, one of the most beautiful hotels in Europe -- and I might add, the best-run in the world? They were spending money! Not rubles, either, bags and bags of real money, the kind they call hard currency. And although nobody in Switzerland seems willing to admit to knowing how these Russians earn their living and where all that money comes from, it doesn't take a rocket scientist to figure it out. I had come face to face with the Russian Mafia. Now this is one of the world's richest shopping streets, so I was on familiar territory when I set out to spy on the Russians. They bought furs, though it was the hottest week Zurich had suffered in decades. They bought watches and more watches with what was to me a unique method of selection, they chose strictly on the weight of gold." **Russell comment:** I've heard that Russia is run by the Mafia and the KGB. Could it be true?

Help! This has been the fourth driest year in California history. Frankly, I forget what rain looks like. I have a large cactus garden in the front of my house, and many of the plants didn't make it through this summer; only the hardiest desert types survived. Last week was the beginning of California's so-called "rainy season." So far, it's been a misnomer.

There's only one boom in California -- building prisons. Since the 1980s Cal has built 16 prisons. Five more are under construction or in the design stage. Officials estimate that 22 more prisons will be needed by the year 2000. Under the "three strikes and you're out" rule, analysts say that the state prison population will double in the next decade, and prison construction costs will rise by \$20 billion. **Russell comment:** Yeah, I'm against crime (I've been mugged twice), but the "three strikes" law isn't going to work. A guy can be put away for life for three non-violent felonies such as being caught three times stealing stuff from Sears or walking around with too much cocaine in his pocket. Bad boys, no question about it -- but a life sentence (costing us \$70,000 a year to incarcerate)?

Hollywood: Screen writer Joe Eszterhas ("Basic Instinct," "Sliver") writes sex-drenched stories and the studios love him. Recently he was paid the highest price ever to write an original screen play from (that's right) an idea -- price **\$2.5 million** upfront. Title of the new script -- "One Night Stand." When you're hot, you're hot.

Gun Control: "This will go down in history. For the first time a civilized nation has full gun registration. Our streets will be safer,

our police more efficient, and the world will follow our lead into the future." -- Adolph Hitler, 1935.

Don't get me started on the Second Amendment. It's an Amendment the liberals would love to get rid of. It allows the citizenry to be armed, which was the specific intention of our Founding Fathers. The Fathers were afraid of the power of government, and, of course, they had plenty of experience with government power, courtesy of the British Crown.

An unarmed populace in the face of an armed government is a helpless populace. Ask the citizenry of Haiti; ask the people of Iraq; ask the Cubans; ask the citizens of any nation under the rule of a dictator. But, you protest, no American government could possibly be a menace to us, the good citizens of a free nation. Yeah, I agree, but I also know that "things can change." When dictators take over, they outlaw three things -- gold, guns and news outlets. Gold allows you to escape, guns allow you to fight and news outlets (TV, radio, newspapers) allow you to know what's going on -- inside and outside the country.

Speaking of news outlets, I firmly believe that one reason Washington politicians are "on the run" is that more Americans are now getting more news -- via TV, radio, FAX, copy machines, cyberspace, satellite and, yes, even via newspapers. When Americans see and hear what's actually going on in Washington and among their "leaders," they want these people OUT. An informed public is a dangerous public -- dangerous to the politicians, that is.

Oh No! Bob Prechter (*Elliott Wave Theorist*, PO Box 1618, Gainesville, GA 30503), in a special report, suggests that baseball could be in "for a 55-year period of decline in public favor." How so? Bob shows a chart of Baseball Stadium Attendance Figures, a chart showing that attendance has moved up in a perfect Fibonacci "five," or three waves up corrected by two down waves. Following the fifth wave, which was terminated this year, baseball attendance has crashed -- triggered, of course, by the baseball strike. Actually, I do think baseball's popularity is on the wane, accentuated by the absurd salaries and the rising popularity of the much more exciting football. Remember, football is the major college sport and, nationally, soccer and basketball are both rising in popularity. Significantly, football and basketball are both sports dominated by black players. And whether you realize it or not, American pop culture is increasingly becoming black culture (and if you have teenagers, as I do, you know what I mean).

I keep getting letters asking how the chelation is going. Last week I got treatment number 34, and I'll probably spread it out to one treatment a month from now on. I continue to get skeptical comments from physicians, but that's OK. If or when the FDA or the AMA says chelation is beneficial, all the docs will reverse their stand. For my own specifics -- the angina (heart pains) which I used to get about every month or so have now almost disappeared; I may get angina once in four months. My cholesterol is down to 200 or below, and my triglycerides (which I have never been able to get down under 250, even with the drug Mevacor) have dropped to 173. Is it all a result of chelation? I suspect so, but, of course, I can't prove it.

Alternative medicine got a shot in the arm when the FDA lost its battle to completely control the sale of vitamins and health supplements. The new bill allows health and vitamin sellers to continue to sell -- they just can't make unsubstantiated claims. And now even physicians agree that there's something to the free radical and antioxidant thesis, and most doctors now recommend the taking of vitamin and mineral supplements. More and more, the docs are moving into the sphere of advocating health, rather than simply treating the disease when it arrives.

GOLD: Everybody is asking, "What's the matter with gold; why can't gold rally above 400?" So what's the answer? Is it (1) not enough inflation? Or is it (2) forthcoming deflation? Or is it (3) manipulation by the central banks? Or is it (4) rising interest rates? Or is it (5) a collapse of the dollar? Or is it (6) that gold tends to move opposite to the stock market, and the Dow has been in a rallying phase?

If I had to guess, I'd say it was either number 2 or number 5. In the last Letter I discussed the case for coming deflation. Of course, this is the last thing you'll read about in the newspapers or in your local broker's handout. The conservative thinking is that we can look for a little inflation, or maybe even a lot of inflation, but very few people are thinking in terms of deflation.

Remember this -- almost all primary bear markets result in a certain amount of deflation. We've already seen that many stocks have been deflated. We know that housing prices have been deflated. We know that the growth in the US and in the world's money supply has been deflating. If the inflation cycle has burned itself out and is now turning down, then the first phase will be "a lack of inflation," and then somewhere ahead we will experience real deflation.

Deflation would be an initial negative for gold. BUT -- what if the dollar itself caves in, and you're facing a different scenario? What could set off a dollar collapse? A dollar collapse could be brought on by an unraveling of the huge credit bubble accompanied by a smash of the massive US debt structure. If we get a dollar meltdown, then gold could go to the moon. All of which bolsters the case for holding gold regardless of whether we face inflation or deflation.

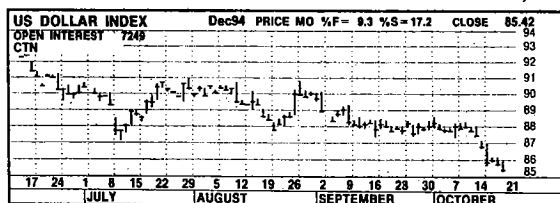
In the last Letter I included a chart showing that the growth rate of G-7 money supply was near a record low. This is certainly not inflationary. You can't have inflation unless you have a torrent of paper chasing real goods. And we haven't got that, not by a long shot.

I also showed that the ratio of US Gross Domestic Product divided by debt is at its highest level since the 1930s. Any decline in GDP would render the massive US debt a "financial nuclear bomb," in other words, the debt would be totally unsustainable -- out-of-control.

So what happens if it turns out that almost all the experts are wrong and the world starts to deflate? As I've explained before, the US today is loaded with \$15.9 trillion of total debt. With that much debt, you simply **cannot withstand deflation**. Which is why I've repeated over and over again -- the US has put itself in a position where it must **"inflate or die."** Die? What do you mean by die? When you're carrying a mountain of debt, deflation is tantamount to dying. If the US deflates, that debt becomes a crushing, unsustainable burden and the currency that the debt is denominated in -- the dollar -- becomes a pariah. Everybody wants out of it. But out to where? To D-marks? Maybe. To Swiss francs? Maybe. To Yen? Maybe. To Gold -- definitely.

All of which brings us to the dollar. Last week we saw the dollar do the financial counterpart of a swan-dive. In a matter of a few days the dollar crashed to its lowest level in two years.

Why? What? How? The answer is probably this -- the US Current Account continues strongly negative. Dollars are flowing out of the US at the rate of \$12 billion a month. To make up for this, we need a foreign torrent of dollars coming into the US. It's not happening. Foreigners are not about to sell their own currencies for dollars (they're up to their necks in dollars now). What about raising interest rates to make the dollar more attractive to hold or to buy? The Fed is reluctant to do it, even though ex-Fed member Wayne Angell shouts that rates should be at least 1% higher in the US (oh, does the Fed hate this Federal Reserve "turncoat").

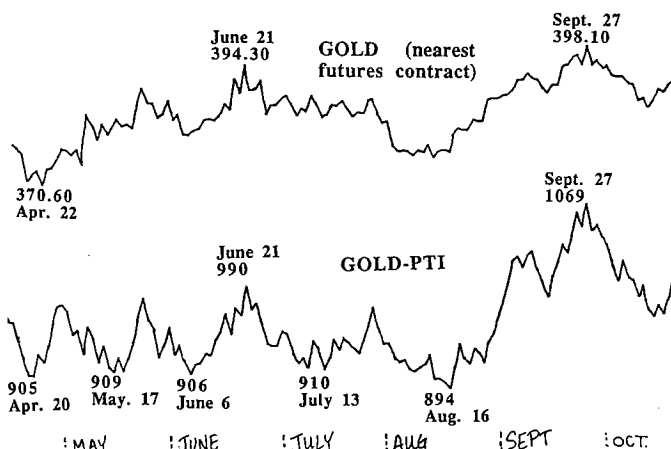


(Dollar chart courtesy of Investor's Business Daily.)

In the meantime the dollar probes the lower depths. It's sinking, sinking, and the worst thing about it is that no one in Washington takes it seriously (but you can bet your life that overseas holders of T-bonds, US stocks and US property take it seriously). At some point (I don't know exactly where) they're going to panic -- meaning that they will SELL.

As to gold and the gold stocks, I believe they are now in "no-man's land." I believe they are floating in that hazy-dazey land where their owners don't know whether the world's fate is to be inflation or deflation, a "good dollar" or a "dead dollar." Gold "feels" cheap here in the 375-400 area. Yet if we're moving towards deflation, gold isn't going to take off on the upside -- not until the big trouble is in sight. That's the way I see it. I realize that I'm not offering subscribers a definite or a satisfactory conclusion. But I've given you everything I know regarding the possible background for gold. But I'll make one prediction and stand on it, and I'll stake whatever reputation I have on it -- gold will outlast the dollar. Gold will be money when the dollar is a museum piece, a relic of the "paper age."

The daily chart shows gold holding its own, but still unwilling to hurdle the 400 level. My Gold-PTI hit its high last December 13 at 1153. It recorded a lower peak on March 25 at 1077. On September 27 it struck a still lower peak at 1069. After backing off moderately into mid-October, the G-PTI is above 975. I'd term the G-PTI action mildly bullish but basically indecisive. A decisive move would be bettering the Sept. 27 peak of 1069. As this is written, 392 units of the collapsing dollar buys an ounce of gold. Extraordinary -- can it last?



LATE NOTES: Oct. 20 -- GM (high was 65 3/8) breaks to a 52-week low of 41 1/4, representing a loss of 38% of its high. GM used to be considered THE market bellwether. Maybe not anymore, but Wall Streeters cringe when GM hits new lows for the year -- that's bear market action.

With the Dow yielding 2.70% and the long Treasury Bond yielding 8%, it's well to remember that the bonds now yield nearly **three times what the Dow yields**. This is "danger city." Classically, it tells us that the Dow is "out-of-whack" with the bonds, meaning that the Dow is too expensive relative to bonds. With the dollar at a two year low and bonds dropping in sync with the dollar, stocks will be under continuing pressure.

In the face of the fading dollar, Treasury Secretary Bentsen saw fit to tell the world that the US has no intention of supporting the dollar. On Bentsen's words the dollar promptly fell further. The next day, sensing his stupid mistake, Bentsen reversed himself. Is Bentsen smoking something we don't know about -- and inhaling?

Parting thought: study the chart on page 2. That chart cuts through all the talk, all the hopes, all the predictions, and it tells a story. The story? Continuing deterioration in the understructure of the stock market.

NEXT MAILING: Nov. 9, 1994